Many multiemployer defined benefit pension plans have been required to develop a funding improvement or rehabilitation plan. This article explains what trustees must do to adopt and implement the plan.
The multiemployer defined benefit fund legal landscape was fundamentally changed just over a decade ago when President George W. Bush signed the Pension Protection Act of 2006 (PPA) into law on August 17, 2006.

One of the most significant changes brought about by PPA was the requirement that trustees of multiemployer defined benefit funds that are less than 80% funded develop either a funding improvement or rehabilitation plan to enhance funding through reductions in benefits, increases in contributions or both. Needless to say, these plans can be challenging to develop, given not only complex and technical advice from fund attorneys and actuaries but also the emotionally charged environments in which they are typically deliberated and the roles of both trustees and bargaining parties in implementation.

This article is intended as a basic overview of the process by which funding improvement and rehabilitation plans are adopted and implemented.¹

Zone Certification and Notification

Within the first 90 days of a plan year, PPA requires that the fund actuary of a multiemployer defined benefit fund certify whether the fund is in endangered or critical status. This has
become known as the zone certification, with each zone generally defined as follows:

- **Green**: Funding percentage\(^2\) of 80% or more
- **Yellow (Endangered)**: Funding percentage under 80% or a projected accumulated funding deficiency\(^3\) in the current or next six plan years
- **Orange (Seriously endangered)**: Funding percentage under 80% and a projected accumulated funding deficiency in the current or next six plan years.
- **Red (Critical)**: Either:
  - Funding percentage under 65% and fails a seven-year solvency test, or
  - An accumulated funding deficiency in the current or next three plan years (four plan years if the funding percentage is under 65%).\(^4\)
- **Critical and declining**: This is a critical plan that is:
  - Projected to become insolvent\(^5\) in the current or next 14 plan years, or
  - Projected to become insolvent in the current or next 19 plan years and either has a ratio of inactive to active participants greater than 2 to 1 or is less than 80% funded.\(^6\)

The Department of Labor (DOL) may assess a penalty of up to $2,063 per day on a plan administrator for failure to timely obtain the required zone certification.\(^7\)

Within 30 days of an endangered or critical zone certification, the trustees must provide a notice of such certification to the participants, beneficiaries, bargaining parties, the Pension Benefit Guaranty Corporation (PBGC) and DOL.\(^8\)

Thereafter, the trustees must proceed to adopt a funding improvement plan for endangered status plans or a rehabilitation plan for critical status plans.

### Endangered Plans (Yellow or Orange)

#### The First Year—Adoption of a Funding Improvement Plan

Within 240 days after the initial certification of endangered status, the trustees must adopt a funding improvement plan (FIP).\(^9\) If the trustees fail to do so, DOL may assess a penalty of $1,296 on the plan administrator for each day the FIP is overdue.\(^10\)

A FIP contains alternative options of benefit reductions, contribution increases or both, designed to meet the following benchmarks:

- **Avoid an accumulated funding deficiency**
- **Increase the funded percentage**: The FIP must be designed so that the projected funded percentage is at least 83.25% at the end of the FIP (75% + (33% × (100% − 75%)) = 83.25%).

There is no limit on the number of options to improve funding that can be in a FIP, but two of these options must be:

- An option for reducing future benefit accruals needed to meet the benchmarks, with no contribution increases unless necessary to meet the benchmarks after future benefit accruals have been reduced to the extent allowed by law (this is known as the default schedule)
- An option for increasing contributions to meet the benchmarks, assuming no reductions of future benefit accruals.\(^12\)

Thirty days after adoption of the FIP, the trustees must provide the various funding options contained in the FIP to the bargaining parties.\(^13\) If the bargaining parties do not adopt one of these options within 180 days of the expiration of the collective bargaining agreement that was
in effect as of the date the plan entered endangered status, then the trustees must impose the default schedule. The default schedule, as mentioned above, provides for the reduction of future benefit accruals to the extent necessary to meet the FIP benchmarks, with no contribution increases unless necessary to meet these benchmarks after future benefit accruals have been reduced to the extent allowed by law. The default schedule, as mentioned above, provides for the reduction of future benefit accruals to the extent necessary to meet the FIP benchmarks, with no contribution increases unless necessary to meet these benchmarks after future benefit accruals have been reduced to the extent allowed by law.

In summary, the first year time line is as follows:

- Day 1: First day of plan year
- Day 90: Actuarial zone certification due
- Day 120: Notice of endangered status due
- Day 330: Trustees deadline to adopt a FIP
- Day 360: Trustees must present FIP to bargaining parties.

Special Rules

It is important to note a few special rules restricting the trustees’ actions once a plan is certified as endangered.

First, between the time the fund actuary certifies endangered status and the adoption of the FIP, the trustees may not:

- Accept a collective bargaining agreement that provides for a reduction in the level of contributions for any participants, a suspension of contributions with regard to any period of service or any new or indirect exclusion of younger or newly hired employees from plan participation or
- In general, amend the plan in any manner that results in an increase in liabilities, unless required by law.

Second, after the adoption of a FIP, the plan document cannot be amended:

- To be inconsistent with the FIP or
- To increase benefits, including future benefit accruals, unless the plan actuary certifies that such increase is paid for out of additional contributions not contemplated by the FIP and, after taking into account the benefit increase, the plan is still reasonably expected to meet the FIP benchmarks.

After the First Year

PPA provides that the plan sponsor must annually update the FIP and file an update with the plan’s annual report (the Form 5500). This includes an update of the schedule of contribution rates to reflect the experience of the plan.

The required action time line for the second year and beyond for a plan in endangered status is as follows:

- Day 1: First day of plan year
- Day 90: Actuarial zone certification due
- Day 120: Notice of endangered status due
- Prior to last day of plan year: Update FIP.

The FIP will remain in place until the plan is no longer in endangered status or has reached the end of the funding improvement period without emerging from endangered status.

Critical Status Plans

The First Year—Adoption of a Rehabilitation Plan

Within 240 days after the initial zone certification of critical status, the trustees must adopt a rehabilitation plan. If the trustees fail to do so, then, just like a delay in timely adopting a FIP discussed above, DOL may assess a penalty of $1,296 on the board of trustees for each day the rehabilitation plan is overdue.

A rehabilitation plan consists of various options, agreed upon by the trustees, setting forth benefit reductions, contribution increases or both to enable the plan to cease to be in critical status by the end of the rehabilitation period. The rehabilitation plan also must provide annual standards for meeting the requirements of the plan.

There is no limit on the options the trustees may adopt in the rehabilitation plan, but one option must be the “default schedule.” The default schedule sets forth reductions in future benefit accruals and other benefits (other than benefits the reduction or elimination of which are not permitted under Internal Revenue Code (IRC) §411(d)(6)) to the maximum extent permitted by law, with contribution increases only to the extent necessary to emerge timely from critical status after such benefit reductions have been made.

Unlike a FIP, the options in the rehabilitation plan may contain reductions in “adjustable benefits.” In general, adjustable benefits are:

- Benefits, rights and features under the plan including postretirement death benefits, 60-month guarantees, disability benefits not yet in pay status and similar benefits
- Any early retirement benefit or retirement-type subsidy and any benefit payment option (other than the qualified joint and survivor annuity)


**takeaways**

- **PPA** requires that within the first 90 days of a plan year, an actuary must certify whether a multiemployer defined benefit plan is in endangered or critical status.
- Trustees of such a plan must notify participants, beneficiaries, bargaining parties, PBGC and DOL within 30 days of the zone certification and must adopt either a FIP or a rehabilitation plan within 240 days.
- Special rules restrict trustees’ actions once a plan is certified as endangered; similar rules and some unique rules apply to trustees’ actions when a plan has been certified as critical.
- The FIP must be updated annually, and it remains in place until the plan no longer is in endangered status or until the end of the funding improvement period.
- Unlike a FIP, a rehabilitation plan may contain reductions in adjustable benefits, with some restrictions and notice requirements, and other unique provisions.
- There still is no comprehensive guidance on developing FIPs and rehabilitation plans; trustees should work closely with plan professionals.

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• Benefit increases made less than 60 months before the first day of the initial critical year.26

There are, however, restrictions on the reduction of adjustable benefits:

• There can be no reduction in adjustable benefits of retirees who entered pay status prior to the date the initial notice of critical status was provided.27

• No reduction can be made unless a notice of reduction in adjustable benefits is provided to all participants, beneficiaries, contributing employers and each employee organization representing plan participants at least 30 days before the reduction takes effect.28

Thirty days after the adoption of the rehabilitation plan, the trustees must provide the rehabilitation plan options to the bargaining parties.29 If the bargaining parties do not adopt one of these options within 180 days of the expiration of the collective bargaining agreement that was in effect as of the date the plan entered critical status, then the trustees must impose the default schedule.30

As noted above, the default schedule reduces future benefit accruals and other benefits (other than benefits the reduction or elimination of which are not permitted under IRC §411(d)(6)) to the maximum extent permitted by law and provides for contribution increases only to the extent necessary to emerge timely from critical status after such benefit reductions have been made.31

**Special Rules**

There are rules restricting trustees’ actions once a plan is certified as critical, some of which are similar to rules applicable to endangered status plans and some unique to critical status plans.

First, similar to a plan in endangered status, between the time the fund actuary certifies critical status and the adoption of a rehabilitation plan, the trustees may not:

• Accept a collective bargaining agreement that provides for a reduction in the level of contributions for any participants, a suspension of contributions with regard to any period of service, or any new or indirect exclusion of younger or newly hired employees from plan participation, or

• In general, amend the plan in any manner that results in an increase in liabilities, unless required by law.32

Second, again similar to a plan in endangered status, after the adoption of a rehabilitation plan, the plan document cannot be amended:

• To be inconsistent with the rehabilitation plan or

• To increase benefits, including future benefit accruals, unless the plan actuary certifies that such increase is paid for out of additional contributions not contemplated by the rehabilitation plan and, after taking into account the benefit increase, the plan is still reasonably expected to meet the benchmarks in accordance with the rehabilitation plan.33

The following provisions, however, are unique to plans in critical status:

• **Employer surcharge:** Sixty days after the actuarial certification, a 5% surcharge is imposed on employer contributions, effective 30 days after the employer has been notified by the plan sponsor that the plan is in critical status and that the surcharge is in effect.34 The surcharge increases to 10% for each plan year after the initial critical year.35 It remains in effect until the contributing employer is party to a collective bargaining agreement (or other agreement, such as a participation agreement) that has been amended to include a schedule consistent with the rehabilitation plan.36

• **Expedited resolution:** If there are less than 60 days before the rehabilitation plan must be adopted and the
trustees cannot agree on a rehabilitation plan, any member of the board of trustees may require that the board enter into an expedited resolution procedure for development of a rehabilitation plan.

- **Payment of lump sums:** Effective on the date of the initial notice of critical status, a plan may not pay benefits in excess of the monthly amount that would be payable under a single life annuity. For the most part, this means no lump-sum benefit may be paid (other than benefits that can be immediately distributed without the consent of the participant, i.e., benefits with a total value of less than $5,000 or certain retroactive payments).

In summary, the time line for an initial critical status year is as follows:

Day 1: First day of plan year
Day 90: Actuarial zone certification due
Day 120: Notice of critical status due
Day 150: 5% employer surcharge imposed on contributions (see above discussion regarding the expiration date of this surcharge)
Day 330: Trustees deadline to adopt a rehabilitation plan
Day 360: Trustees must present rehabilitation plan to bargaining parties.

**After the First Year**

PPA provides that the plan sponsor must annually update the rehabilitation plan and file an update with the plan’s annual report (the Form 5500). This includes an update of the schedule of contribution rates to reflect the experience of the plan.

After the initial critical year certification, each subsequent certification while a plan is in critical status must also include whether the actuary certifies the plan is making scheduled progress. If the actuary fails to certify scheduled progress for three years in a row, the plan will be treated as having a funding deficiency subject to excise taxes under the IRC.

The required action time line for the second year and beyond for a plan in critical status is as follows:

Day 1: First day of plan year
Day 90: Actuarial zone certification due
Day 120: Notice of critical status due
Prior to last day of plan year: Update rehabilitation plan.

The rehabilitation plan ends once the actuary certifies that the plan has emerged from critical status.

**Conclusion**

The basic framework and requirements of PPA, set forth above, are fairly straightforward, but there remain several provisions subject to reasonable, differing interpretations. To date, a decade after PPA’s enactment, there still are no comprehensive regulations to provide guidance. Therefore, care must be taken in developing any funding improvement or rehabilitation plan, and trustees are advised to work closely with plan professionals in doing so.

**Endnotes**

1. References in this article are to the Pension Protection Act of 2006, as modified by the Multiemployer Pension Reform Act of 2014 (MPRA).
2. In general, the funded percentage for PPA purposes is the actuarial value of assets divided by accrued liability.
3. In simple terms, an accumulated funding deficiency means that minimum required contributions have not been made to a plan over time.
4. In addition, the board of trustees of a plan that is not in critical status in the current plan year but is projected by the plan actuary to be in critical status in the succeeding five plan years may elect to be in critical status effective the current plan year. This election must be made not later than 30 days after the zone certification.
5. IRC §432(b)(4).
6. A plan is insolvent when it no longer has money to pay benefits and expenses currently due.
7. IRC §432(b)(6).
8. IRC §432(b)(3)(C); Employee Retirement Income Security Act (ERISA) §502(c)(2). This amount previously was $1,100 per day. The Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 increased this penalty for violations occurring after November 2, 2015 and assessed after August 1, 2016. Beginning in 2017, this amount will be adjusted annually by January 15.
9. DOL provides a model notice of critical status but does not provide a model notice of endangered status. The model notice of critical status and sample notices of endangered status can be found at www.dol.gov/ebsa/criticalstatustnotices.html.
10. Note that a plan that otherwise meets the definition of endangered is not required to adopt a funding improvement plan if in the prior plan year it was neither endangered nor critical and in the current plan year the actuary projects that without taking any action (i.e., no benefit decreases and no contribution increases), the plan is projected to no longer be in endangered status in ten years. Prior to MPRA, such a plan would at least adopt a “no action” FIP, but MPRA made this unnecessary. A plan in this situation is, however, required to provide notice that it is in endangered status but for these certifications to the bargaining parties and PBGC. See IRC §432(b)(3)(D)(iii), (S).
11. ERISA §502(c)(8). This amount previously was $1,100 per day. The Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 increased this penalty for violations occurring after November 2, 2015 and assessed after August 1, 2016. Beginning in 2017, this amount will be adjusted annually by January 15.
12. IRC §432(c)(1)(B); §432(c)(7)(A).
13. IRC §432(c)(1)(B).
14. Once a schedule of contribution rates is adopted, a failure to pay contributions under a FIP (whether such contributions are in place because they were affirmatively adopted by the bargaining parties or imposed by default) is treated as a delinquent contribution under ERISA §515. ERISA §305(c)(7). Further, the failure of an employer to make required contributions under a FIP triggers an excise tax on the delinquent contributions equal to 100% of the contribution owed. See IRC §4971(g)(2).
15. IRC §432(c)(7)(A).
16. This time line assumes the maximum time allowed by law is taken to complete each step.
17. IRC §432(d)(2).
18. IRC §432(d)(1). Prior to MPRA, during the funding improvement period, which includes time after the adoption of the FIP, the plan sponsors of an endangered status plan could not accept a collective bargaining agreement that provided for a reduction in the level of contributions for any participant, a suspension of contributions with regard to any period of service, or any new or indirect exclusion of younger or newly hired employees from plan participation. This restriction was limited to the funding adoption period by MPRA, with the result that these restrictions for endangered status plans are now consistent with similar rules applicable to critical status plans. See IRC §§432(d) and (e).
19. IRC §432(c)(6)(A), (B).
20. Thus, a funding improvement plan would end if:
   • The plan is certified as green
   • The plan fails to emerge from endangered status at the end of the funding improvement period, in which case the FIP would continue in effect until a new FIP is adopted, or
   • The plan is certified as critical, in which case the funding improvement period would close at the end of the plan year immediately preceding the first critical status year. IRC §§432(c)(4)(C), (D).
21. ERISA §502(c)(8). See endnote 10, above.
22. The rehabilitation period is a ten-year period beginning on the first day of the first plan year of a multiemployer plan following the earlier of the second anniversary of the date of the adoption of the rehabilitation plan or the expiration of the collective bargaining agreements covering at least 75% of active participants in effect on the due date for the actuarial certification for the initial critical year. IRC §§432(e)(3)(A)(i), (4). If the trustees determine that, based on reasonable actuarial assumptions and upon exhaustion of all reasonable measures, the plan cannot reasonably be expected to emerge from critical status during this ten-year period, then the rehabilitation period is that period of time necessary to emerge from critical status at a later date or to forestall possible insolvency. IRC §432(e)(3)(A)(ii).
23. IRC §432(e)(3). PPA fails to explicitly define the “annual standards” that must be met.
24. IRC §432(e)(1). The default schedule in the rehabilitation plan has a limit on the reduction in future accruals. Any reduction in the rate of future accruals under the default schedule of a rehabilitation plan cannot reduce the rate of future accruals below the lower of the accrual rate already in the plan or a monthly benefit payable as a single life annuity commencing at normal retirement age equal to 1% of the contributions required to be made with respect to a participant. IRC §432(e)(6).
25. IRC §432(e)(8)(A)(ii). MPRA added provisions to PPA also allowing, under very specific circumstances, a plan in critical and declining status to suspend benefits. Suspending benefits under MPRA means the temporary or permanent reduction of any current or future payment obligation; i.e., it allows the reduction of accrued benefits for both active and retired participants. Among other things, a suspension of benefits cannot take place until the plan has submitted and received approval of an application to do so from the Department of Treasury. A discussion of the conditions under which benefits may be suspended is beyond the scope of this article. See IRC §432(e)(9).
26. IRC §432(e)(8)(A)(iv). Except for benefit increases that would not be eligible for PBGC protection, the rehabilitation plan options cannot reduce a participant’s accrued benefit payable at normal retirement age. IRC §432(e)(8)(B).
27. IRC §432(c)(8)(A)(ii).
28. IRC §432(e)(8)(C).
29. IRC §432(c)(1)(B).
30. Once a schedule of contribution rates is adopted, a failure to make contributions under a rehabilitation plan, whether such contributions are adopted affirmatively or by default, is treated as a delinquent contribution under ERISA §515. ERISA §305(c)(7). Further, the failure of an employer to make required contributions under a FIP that is in effect triggers an excise tax on the delinquent contributions that is equal to 100% of the contribution owed. See IRC §4971(g)(2).
31. IRC §§432(e)(3)(C), (1).
32. IRC §432(f)(3).
33. IRC §432(f)(1).
34. IRC §432(e)(7)(A). The DOL model notice of critical status contains a notice to contributing employers regarding this surcharge.
35. IRC §432(e)(7)(A).
36. IRC §432(e)(7)(C).
37. ERISA §305(h).
38. IRC §432(f)(2).
39. This time line assumes the maximum time allowed by law is taken to complete each step.
40. IRC §432(e)(3)(B)(i) and (ii).
41. IRC §§4971(a), (b), (g)(3).
42. IRC §432(e)(4)(A). Under PPA prior to MPRA, the test for emerging from critical status differed from the triggers that caused a plan to enter critical status—particularly in the use of amortization extensions, which created a situation where a plan could exit and then immediately reenter critical status—the so-called revolving door. MPRA modified the rules for emergency to help eliminate this revolving door. See IRC §432(e)(4)(B).